

1 Tara J. Schleicher, OSB #954021
2 tschleicher@fwwlaw.com
3 Farleigh Wada Witt
4 121 SW Morrison Street, Suite 600
5 Portland, Oregon 97204-3136
6 Telephone: (503) 228-6044

7 Attorneys for Debtor

8 IN THE UNITED STATES BANKRUPTCY COURT
9 FOR THE DISTRICT OF OREGON

10 In re

11 Salpare Bay, LLC,

12 Debtor.

Case No. 10-35333-tmb11

DEBTOR'S REPLY TO STOEL RIVES'
OBJECTION TO MOTION TO OBTAIN
CREDIT

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14 Salpare Bay, LLC ("Debtor") hereby replies to Stoel Rives' Objection to Motion
15 to Obtain Credit ("the "Objection"). Stoel Rives' Objection should be overruled for the
16 following reasons: (1) Stoel Rives has waived the right to object to the proposed Debtor-in-
17 Possession financing (the "DIP Loan"); (2) Stoel Rives has an unwaivable conflict that prohibits
18 Ms. Kosydar from representing it with respect to the Objection or any objection to the
19 confirmation of the Debtor's Third Amended Plan of Reorganization (the "Plan"); and (3) Stoel
20 Rives' Objection is not an objection to the Debtor's Motion to Obtain Credit ("the Motion"), but
21 an objection to plan confirmation, which can only be properly addressed at confirmation. For all
22 of these reasons, the Court should overrule Stoel Rives' Objection.

23 1. **Stoel Rives Waived its Right to Object to the DIP Loan.**

24 On May 5, 2011, the Debtor filed with this Court a Notice of Intent to Settle and
25 Compromise (Docket No. 229) (the "Notice of Intent"), which set forth the terms of the
26 Settlement Agreement between the Judgment Creditors (as that term is defined in the Settlement

1 Agreement) and the Debtor. On the same day, the Debtor served the Notice of Intent on all
 2 interested parties on the mailing matrix, including Stoel Rives.

3 The Notice of Intent clearly disclosed that the DIP Loan is a material element of
 4 the Debtor's settlement agreement to be approved by the court. The Notice of Intent stated (1)
 5 the amount of the DIP Loan that would be sought, (2) that a priming lien would be sought to
 6 secure the DIP Loan, (3) the timing of the Debtor obtaining the DIP Loan (prior to confirmation),
 7 (4) the purposes for which the DIP Loan proceeds would be used, and (5) all of the salient terms
 8 of the DIP Loan relevant to the Objection that Stoel Rives now attempts to make.

9 The objection period for the Notice of Intent expired on May 26, 2011. No
 10 objections were filed. Most relevant to the matter before this Court, Stoel Rives filed no
 11 objection to the Notice of Intent. This Court approved the Settlement Agreement and authorized
 12 the Debtor and Judgment Creditors to carry out the terms of the Settlement Agreement by order
 13 entered June 13, 2011 (Docket No. 237). As set forth above, the Notice of Intent clearly and
 14 undeniably set forth the fact that the DIP Loan was an integral part of the Settlement Agreement
 15 for which the Debtor sought approval to enter with the Judgment Creditors. Any objection that
 16 Stoel Rives had to the Debtor seeking the DIP Loan secured by a priming lien should have been
 17 raised prior to May 26, 2011. Stoel Rives made no such objection. Therefore, it has waived the
 18 right to object to the DIP Loan, which is the lynchpin of the Settlement Agreement. This Court
 19 should deny its Objection to the Motion on that basis alone.

20 **2. Stoel Rives' unwaivable conflict of interest prohibits it from litigating**
 21 **the Objection with current counsel.**

22 Pursuant to Oregon Rule of Profession Conduct 1.9 (a) (Duties to Former Clients)
 23 "[a] lawyer who has formerly represented a client in a matter shall not thereafter represent
 24 another person in the same or a substantially related matter in which that person's interests are
 25 materially adverse to the interests of the former client unless each affected client gives informed
 26 consent, confirmed in writing." A matter-specific conflict under Rule 1.9(a) merely involves the

1 same transaction or legal dispute with the main concern being disloyalty to the former client. *In*
 2 *re Conduct of Hostetter*, 348 Ore. 574, 591 (Or. 2010) (citing ABA/BNA Lawyers' Manual on
 3 Professional Conduct § 51:226). Generally "current representation adverse to a former client is
 4 substantially related to the earlier representation if it involves the lawyer's own work for the
 5 former client -- especially an attack on that work." *Id.*; see also Restatement of Law Governing
 6 Lawyers § 132(1) (2000) (a current matter is substantially related to an earlier matter if "the
 7 current matter involves the work the lawyer performed for the former client"). See also DR 5-
 8 105(C) (Except as permitted by DR 5-105(D), a lawyer who has represented a client in a matter
 9 shall not subsequently represent another client in the same or a significantly related matter when
 10 the interests of the current and former clients are in actual or likely conflict).

11 In its Objection, Stoel Rives acknowledges that it represented the Debtor pre-
 12 petition and post-petition by "providing assistance to debtor's bankruptcy professionals to obtain
 13 a timely filing of this case and in the prosecution of the claims against the construction lien
 14 holders". Declaration Of Christine A. Kosydar In Support Of Stoel Rives LLP'S Objection To
 15 Debtor's Motion To Obtain Credit (Docket No. 247). Stoel Rives considered this work "an
 16 investment in [the] Debtor's bankruptcy". *Id.* Moreover Stoel Rives touts its pre and post
 17 petition legal work on behalf of the Debtor which resulted in "considerable" advantages for the
 18 Debtor. Indeed, Stoel Rives takes the position that, but for Stoel Rives, the "Debtor would not
 19 be here." Despite its diligent legal efforts both pre and post petition to protect and advance the
 20 interests of the Debtor, Stoel Rives now takes a materially adverse position to the Debtor on the
 21 exact same matter and issues in which Stoel Rives provided recent legal representation.

22 The Debtor does not dispute Stoel Rives' right to protect its unsecured claim for
 23 accrued prepetition attorney fees. The Debtor does not contend, for example, that Stoel Rives
 24 could not seek a higher payment percentage on its unsecured claim like any other unsecured
 25 creditor. However, Stoel Rives is not merely seeking alternate plan treatment which would
 26 ensure a greater dividend on its claim. Rather, notwithstanding its prior "successful legal work

1 and strategies” for the benefit of the Debtor’s reorganization, Stoel Rives now seeks a complete
2 liquidation of the Debtor, which according to financial projections would result in zero payment
3 to unsecured creditors, including Stoel Rives. Stoel Rives attempts to circumvent this fact by
4 alleging, despite prior court rulings, liquidation value in property sufficient to pay unsecured
5 interests. This position is incorrect and wholly unsupported by the facts. Stoel Rives’ Objection
6 and desire to force a liquidation of the Debtor is no more than an attempt to strong arm the
7 Debtor into a guarantee of a 100% payment for unsecured pre petition attorney fees to the
8 detriment of the Debtor. Stoel Rives apparently would prefer to receive zero cents on the dollar
9 through liquidation than a potential reduced payment on its claim. If Stoel Rives could
10 successfully object to confirmation and force a conversion of the Debtor, it will have effectively
11 ruined the Debtor and its reorganization, which Stoel Rives previously stated to be on a
12 successful course due to its legal efforts. Stoel Rives attacks its own work in assisting pre and
13 post confirmation with the reorganization of its former client. The position now taken by Stoel
14 Rives in this bankruptcy is in direct conflict with the positions previously taken until this point in
15 time. This is confirmed by Stoel Rives’ failure to object to the Notice of Intent as discussed
16 above.

17 Stoel Rives is barred by the Oregon Rules of Professional Conduct from
18 representing itself in seeking a liquidation of the Debtor. The posture of Stoel Rives goes
19 beyond the acts of a typical unsecured creditor diligently enforcing its claim in a bankruptcy. No
20 position could be more materially adverse to a former client than the position now taken by this
21 creditor in attacking the ability of its former client to reorganize. The Debtor has not waived this
22 conflict but rather it directly raised the issue of this conflict with Stoel Rives. Based on this lack
23 of consent, Stoel Rives must be barred from representing itself in litigating this issue.

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1 3. **Stoel Rives' arguments are confirmation issues, not properly before**
 2 **the Court at this juncture.**

3 Stoel Rives' arguments in its Objection are really confirmation issues, not issues
 4 to be addressed in conjunction with the Debtor's Motion for approval of the DIP Loan. Stoel
 5 Rives' contentions regarding the treatment of unsecured claims, including its own, have nothing
 6 to do with the Motion and are inaccurate. In fact, some of Stoel Rives' assertions contradict the
 7 proposed Plan provisions. For example, Stoel Rives' contends that the Debtor does not propose
 8 to refinance the Marina. The Plan provides at Page 20, ll.10 that the Debtor will refinance the
 9 Marina and use those proceeds to pay creditors' claims and develop the Property so that it can
 10 generate the Net Income needed to pay unsecured claims.

11 Additionally, Stoel Rives asserts that the Debtor makes no provision for
 12 unsecured creditors if the Plan projections are inaccurate. That is incorrect. Under the proposed
 13 Plan, the Debtor must pay at least 10% of the Unsecured Creditors' Allowed Claims *even if* its
 14 projections regarding Net Income are inaccurate. (Page 15, ll. 24 of the Plan).

15 Lastly, the Objection fails to recognize that all unsecured creditors could receive
 16 100% payment of their Allowed Claims if the Debtor's Net Income exceeds the projections. In
 17 other words, the Debtor does not limit the payment to Unsecured Creditors with a ceiling
 18 percentage.

19 Contrary to the contention in the Objection, Mr. DeFrees is providing new value
 20 for the retention of his membership interests in the Debtor. Mr. DeFrees is subordinating his
 21 \$10.9 million claim to all unsecured creditors' claims. Mr. DeFrees' subordination is a real
 22 contribution that is "necessary to the successful implementation of a feasible plan." *In re*
 23 *Elmwood, Inc.*, 182 B.R. 845, 852-853 (D. Nev. 1995) (citations omitted)(defining "new value"
 24 as a "substantial contribution" and defining "substantiality" as a contribution that is "real and
 25 necessary to the successful implementation" of the plan). *In re Elmwood* is a single asset real
 26 estate case. In that case, the court concluded that a contribution worth "less than 4% of the

unsecured debt discharged in the plan” was substantial and constituted “new value” because it facilitated continued development of the debtor’s property. *Id.* In this case, Mr. DeFrees’ subordination facilitates a plan that provides at least a 10% payment of unsecured claims. The plan would simply not be possible without Mr. DeFrees’ subordination. Like *Elmwood*, Mr. DeFrees’ subordination provides substantial new value and facilitates continued development of the property.

The Objection criticizes the liquidation analysis the Debtor attached to the Disclosure Statement, arguing that the Property has a value of \$12 million. However, what Stoel Rives ignores is this Court’s determination on the value of the Property after the relief from stay hearing at a little over \$9 million (Docket No. 86). Stoel Rives also ignores the costs of sale and the discount on value that a liquidation of the Property would dictate. As set forth in the Debtor’s liquidation analysis, the ultimate payout to unsecured creditors would be zero under a chapter 7 scenario. The Debtor’s proposed plan is definitely in all of the creditors’ best interests.

With all of that having been said, all of these issues raised by Stoel Rives are properly addressed at confirmation, not at the hearing on the Motion for approval of the DIP Loan.

CONCLUSION

This Court should overrule Stoel Rives’ Objection to the Motion because it waived its right to object to the DIP Loan, a central component of the Settlement Agreement by failing to file an objection to the Notice of Intent. Its arguments in the Objection should be heard

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1 at confirmation, not at this juncture. For all of the foregoing reasons, this Court should overrule
2 Stoel Rives' Objection.

3 Dated: June 23, 2011.

4 FARLEIGH WADA WITT

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6 By: /s/ Tara J. Schleicher
Tara J. Schleicher, OSB #954021
7 tschleicher@fwwlaw.com
(503) 228-6044
8 Of Attorneys for Debtor
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CERTIFICATE OF SERVICE

I hereby certify that on June 23, 2011, I served a copy of **DEBTOR'S REPLY TO STOEL RIVES' OBJECTION TO MOTION TO OBTAIN CREDIT** on the parties listed below as "Non-ECF Participants" by mailing a copy thereof in a sealed, first-class postage prepaid envelope, addressed to each party's last-known address and depositing in the U.S. mail at Portland Oregon.

NON-ECF PARTICIPANTS

Salpare Bay, LLC
2501 NE 134th Street #300
Vancouver, WA 98686

Campbell Crane
8001 NE 14th Pl.
Portland, OR 97211

Acme Construction Supply
330 SE Salmon St.
Portland, OR 97214

Portland General Electric
PO Box 4404
Portland, OR 97208

URS Corporation
PO Box 121028
Dept. 1028
Dallas, TX 75312

Fusion Partners
1801 N. Lamar St.
Dallas, TX 75202

Team Builder JLS
14205 SE 36th St.
Ste. 200
Bellevue, WA 98006

Jordan Schrader Attorneys
PO Box 230669
Portland, OR 97281

Portland Monthly
234 SW Broadway
Portland, OR 97205

Landerholm Memovich Lansverk
PO Box 1086
Vancouver, WA 98666-1086

Professional Serv. Industries
6032 N. Cutter Circle #480
Portland, OR 97217

Bee Consulting
1638 NW Riverscape St.
Portland, OR 97209-1834

City of Portland
City Attorney's Office
Attn: Linda Law
1221 SW 4th Ave., Rm. 430
Portland, OR 97204

Paradigm Communications
PO Box 65229
Seattle, WA 98155

Intelligent Community Services
3303 SW Bond Ave.
Portland, OR 97239-4501

Interspace Airport Advertising
4635 Crackersport Rd.
Allentown, PA 18104

Fountain Technologies
5673 SW Cheltenham Dr.
Portland, OR 97239

Ford Graphics
1431 NW 17th Ave.
Portland, OR 97209

W&H Pacific
9755 SW Barnes Rd. #300
Portland, OR 97225

KPFF Consulting
111 SW Fifth Ave., Suite 2500
Portland, OR 97204

Dated: June 23, 2011.

FARLEIGH WADA WITT

By: /s/ Tara J. Schleicher
Tara J. Schleicher, OSB #954021
tschleicher@fwwlaw.com
Of Attorneys for Debtor